

MEMORANDUM

To: City Council Finance Committee Date: September 25, 2012

From: Lauren Bradley, Finance and Management Services Director

Subject: Auditor Procurement Policy and RFP for audit services

Best Practices

The Government Finance Officer's Association (GFOA) has made the following recommendations, among others, regarding the selection of auditing services:

- Governmental entities should enter into multiyear agreements of at least five years in duration when obtaining the services of independent auditors. Such multiyear agreements can take a variety of different forms (e.g., a series of single-year contracts) and allow for greater continuity and help minimize the potential for disruption in connection with the independent audit. Multiyear agreements can also help to reduce audit costs by allowing auditors to recover certain "startup" costs over several years, rather than over a single year.
- Governmental entities should undertake a full-scale competitive process for the selection of independent auditors at the end of the term of each audit contract, consistent with applicable legal requirements. Ideally, auditor independence would be enhanced by a policy requiring that the independent auditor be replaced at the end of the audit contract, as is often the case in the private sector. Unfortunately, the frequent lack of competition among audit firms fully qualified to perform public-sector audits could make a policy of mandatory auditor rotation counterproductive. In such cases, it is recommended that a governmental entity actively seek the participation of all qualified firms, including the current auditors, assuming that the past performance of the current auditors has proven satisfactory.

History

The City of Asheville has utilized Dixon Hughes Goodman LLP (Dixon Hughes) for auditing services for the last seven fiscal years under single-year contracts. The City retained the services of Martin Starnes & Associates for the FY 2004-2005 fiscal year audit and utilized Crisp Hughes Evans for several years prior to FY 2005. Crisp Hughes Evans merged with a Dixon Hughes predecessor firm in 2004.

The City's long term relationship with Dixon Hughes is likely related to several factors, including the fact that it is the largest CPA firm in the southeast with a local office in Asheville. During the last four years, Dixon Hughes worked with Asheville as the City transitioned to a more complex financial system through the implementation of the enterprise resource planning (ERP) software Munis. At the same time, the City's Finance Department experienced staff turn over in key positions, and continuity in the independent auditor's role has been essential to timely completion of the audit. As a result, Dixon Hughes has extensive experience auditing the City's financial systems, accounts and records, including valuable insight and understanding of the financial system's processes and controls.

In 2011, City Council expressed an interest in pursuing a competitive process for the selection of independent auditors. Staff was prepared to launch a Request for Proposals (RFP) but requested that the City delay the RFP process for an additional year to permit a relatively new team in the Finance Department the optimal opportunity to complete the audit by October 31, 2012, a deadline that was adopted by City Council as part of the City's Financial Policy.

City Council approved staff's recommendation, and the services of Dixon Hughes were retained for a single, final year to conduct the audit of the city's accounts for the fiscal year ending June 30, 2012. Staff recommended that the City issue an RFP in the November/December 2012 timeframe for audit services for FY 2013.

City of Asheville Financial Policy

Staff believes an RFP for audit services would generate sufficient competition among firms due to the size, scope and duration of the engagement. Given GFOA's recommended best practices, staff recommends City Council adopt the following statement as part of the City's Financial Policy:

Auditor Procurement Policy: When obtaining the services of independent auditors, the City of Asheville shall enter into multiyear agreements of at least five years in duration through a series of single-year contracts as consistent with North Carolina State law. The City shall undertake a full-scale competitive process for the selection of independent auditors at the end of the term of each audit contract, consistent with applicable legal requirements. It is the City of Asheville's policy that the independent auditor be replaced at the end of the five-year engagement to enhance auditor independence unless lack of competition among audit firms fully qualified to perform public-sector audits make mandatory rotation counterproductive. The principal factor in the selection of an independent auditor is the auditor's ability to perform a quality audit. In no case should price be allowed to serve as the sole criterion for the selection of an independent auditor.

If adopted, the City's current audit service firm could not compete in the RFP process for FY13 since it has been working with the City for a period greater than five years.

Timeline

- RFP development and release: November 2012
- Staff evaluation of responses: December 2012
- Finance Committee review: January 2013
- Contract award: February 2013

Fiscal and Time Resource Impact

Transitioning to a new audit firm will require additional time to get the auditors familiar with Asheville's financial systems, processes and controls. As illustration, according to a survey of the public accounting firms and Fortune 1000 public companies (United States General Accounting Office 2003), auditors' initial year audit costs increase by more than 20 percent over subsequent year costs to acquire the necessary knowledge of the client. In addition, their marketing costs also increase by more than 1 percent. Additionally, the survey found that clients

will incur additional auditor selection costs and auditor support costs of at least 17 percent of initial-year audit fees.

For FY 2012, the City of Asheville executed an audit contract with Dixon Hughes for \$109,000. Staff would estimate that the first year of an engagement with a new firm would range from \$110,000-\$145,000.

Staff Recommendation

Staff recommends the Finance Committee approve the Auditor Procurement Policy and forward its consideration to the full City Council at its October 9, 2012 meeting. If it is approved, staff will begin to develop an RFP for audit services for FY13 according to the timeline presented above.